

WILLIAM A. MUNDELL
Chairman
JIM IRVIN
Commissioner
MARC SPITZER
Commissioner

**NOTICE OF OPPORTUNITY FOR HEARING
REGARDING PROPOSED ORDER TO
CEASE AND DESIST, FOR RESTITUTION,
FOR ADMINISTRATIVE PENALTIES, FOR
REVOCATION OR SUSPENSION, AND FOR
OTHER AFFIRMATIVE ACTION**

3. From on or about February 17, 1994, until April 6, 2001, MERRILL was registered as a securities salesman in Arizona with Morgan Stanley Dean Witter, Inc. (“MSDW”). While with MSDW, MERRILL worked at the branch office in the Sun City, Arizona area. In April 2001,

1 MERRILL was terminated for alleged unauthorized transactions in a client's account. All
2 allegations contained in this Notice of Opportunity for Hearing occurred while MERRILL was
3 registered with MSDW.

4 4. From on or about May 25, 2001, until November 19, 2001, MERRILL was registered as
5 a securities salesman in Arizona with The Advisors Group, Inc. While with The Advisors Group,
6 Inc., MERRILL worked at the branch office in Phoenix, Arizona. MERRILL was terminated from
7 The Advisors Group, Inc. for failing to comply with heightened supervisory requirements.

8 5. Pursuant to A.R.S. § 44-1949, MERRILL'S registration as a securities salesman in
9 Arizona was automatically suspended on the date of his termination by The Advisors Group, Inc.,
10 on or about November 19, 2001. Since that date, MERRILL has not been registered with any
11 securities dealer. Therefore, pursuant to A.R.S. § 44-1947(B), MERRILL'S registration expired on
12 December 31, 2001. The Commission has the statutory authority pursuant to A.R.S. § 44-1963(D)
13 and A.R.S. § 44-1947(D), to bring this action to suspend or revoke MERRILL'S registration as an
14 Arizona securities salesman within two years after the termination or lapse of his registration.

15 6. Since on or about May 25, 1994, MERRILL has been licensed in Arizona to sell life and
16 variable life insurance products. Both of these insurance licenses expire on February 28, 2002,
17 unless renewed.

18 III.

19 FACTS

20 Customer One

21 7. Customer One is a 78-year-old retired widow who lives in Sun City, Arizona.
22 Customer One had three accounts with MSDW. The primary investment objectives listed with
23 MSDW for Customer One were income and capital appreciation. Customer One's investment
24 goals were conservative. Customer One's sole source of income, other than any investment
25 income she received, was monthly social security payments. Customer One's financial
26 information listed with MSDW was: income of \$7,000 per year, net worth of \$130,000, and

1 liquid assets of \$28,000. Customer One desired preservation of her investment principal due to
2 her age and financial situation. Customer One never signed a discretionary agreement with
3 MSDW and MERRILL.

4 8. From approximately January 1996 to January 1999, MERRILL was Customer One's
5 stockbroker at MSDW. Customer One was not a sophisticated investor. Prior to becoming a
6 customer of MERRILL'S, Customer One's investment experience consisted of investing in bank
7 issued certificates of deposit. Customer One trusted MERRILL and relied upon his financial
8 knowledge and advice. Customer One did not understand the securities statements and other
9 securities-related documents she received from MSDW.

10 9. On a number of occasions, MERRILL requested Customer One sign a discretionary
11 agreement. Despite Customer One's refusal to sign a discretionary agreement, MERRILL treated
12 Customer One's accounts as discretionary accounts. MERRILL conducted several unauthorized
13 trades in Customer One's accounts while he was her stockbroker.

14 10. In approximately January 1998, while having her 1997 taxes prepared, Customer One
15 discovered that MERRILL had sold some of her General Electric stock without her authorization.
16 Soon after discovering this unauthorized trade, Customer One told MERRILL, in his office, that
17 he was not to make any more trades in her accounts without her prior approval. Customer One
18 later found out that MERRILL had conducted other unauthorized trades in her accounts prior to
19 selling her General Electric stock, and that he continued to conduct unauthorized trades in her
20 accounts after this incident.

21 11. Short-term trading often occurred in Customer One's accounts. On a number of
22 occasions, securities, predominantly mutual funds, were sold within two years after being
23 purchased. Mutual funds are considered to be long-term investments.

24 12. During much of 1997 and 1998, the MSDW High-Yield Securities Fund, a mutual
25 fund, represented approximately 40% of Customer One's securities portfolio. This mutual fund
26 seeks a high level of current income with capital appreciation as a secondary objective. The fund

1 invests at least the majority of its assets in high-yield corporate bonds that are below investment
2 grade quality. These are risky bonds with poor credit ratings or even no ratings. The fund
3 maintains no minimum credit-quality restrictions for its investments. The fund is rated a high-
4 risk fund and is otherwise known as a junk bond mutual fund. The share price of the MSDW
5 High-Yield Securities Fund declined during the time period Customer One owned its shares. The
6 MSDW High-Yield Securities Fund was previously called Dean Witter High-Yield Securities
7 Fund.

8 13. Customer One's investment in the MSDW High-Yield Securities Fund was not
9 suitable for her, given the risky nature of the bonds held in that fund, the high concentration of
10 the fund in Customer One's securities portfolio, her investment objectives, her desire to preserve
11 her investment principal, her financial situation and needs, her age, and other relevant factors. In
12 addition, the short-term trading that often occurred in Customer One's accounts, predominantly
13 in mutual funds, was not suitable for Customer One due to the fact that mutual funds are typically
14 long-term investments, and due to Customer One's financial situation and needs, her age, and
15 other relevant factors.

16 Customer Two

17 14. Customer Two is an 83-year-old retired widow who lives in Scottsdale, Arizona.
18 Customer Two had one account at MSDW. Customer Two moved to Arizona in the early 1990's
19 and transferred her account to the Sun City area MSDW branch where MERRILL was assigned
20 as her stockbroker. The investment objective listed on Customer Two's new account form is
21 "aggressive income." Customer Two did not prepare that new account form nor did she
22 understand what "aggressive income" was in relation to investments. Customer Two did not
23 provide any financial information to MSDW such as her net worth and liquid assets. Customer
24 Two never signed a discretionary agreement with MSDW and MERRILL.

25 15. Ever since Customer Two moved to Arizona her sole source of income has been
26 monthly social security payments of approximately \$700. The assets in Customer Two's account

1 represented virtually all of her total net worth. Customer Two did not want to risk loss of her
2 investment principal.

3 16. Customer Two was not a sophisticated investor. Customer Two had no investment
4 training. Customer Two trusted MERRILL and relied upon his financial knowledge and advice.
5 Customer Two did not completely understand the securities statements and other securities-
6 related documents she received from MSDW.

7 17. MERRILL treated Customer Two's account as a discretionary account. MERRILL
8 did not discuss his recommended trades and receive authorization from Customer Two before
9 making the trades mentioned below in her account.

10 18. From approximately January 1998 to July 2000, the MSDW High-Yield Securities
11 Fund represented a range of about 72% to 88% of Customer Two's securities portfolio. The
12 investment objectives and a brief description of this fund are included above for "Customer
13 One." The value of the MSDW High-Yield Securities Fund in Customer Two's account
14 decreased about \$20,000 during this same time period. The only other securities in Customer
15 Two's account during this time period were preferred stocks in one company.

16 19. In or about August 2000, the shares in the MSDW High-Yield Securities Fund were
17 exchanged for shares in the MSDW Information Fund. The MSDW Information Fund seeks
18 long-term capital appreciation. This fund is categorized as a Specialty-Technology fund and has
19 a high-risk rating. The shares in MSDW Information Fund were only held from in or about
20 August 2000 until December 2000 when they were exchanged for shares in another MSDW
21 mutual fund. During this time period, the MSDW Information Fund represented a range of about
22 73% to 81% of Customer Two's securities portfolio. The value of the Information Fund in
23 Customer Two's account declined during the time it was held. The only other securities in
24 Customer Two's account during this time period were preferred stocks in one company.

25 20. In or about December 2000, the shares in MSDW Information Fund were exchanged
26 for shares in MSDW Health Sciences Fund, another mutual fund. Theses shares were held in

1 Customer Two's account until at least October 2001. The MSDW Health Sciences Fund seeks
2 capital appreciation. The fund is categorized as a Specialty-Health fund and has an average-risk
3 rating.

4 21. From in or about December 2000 to October 2001, the MSDW Health Sciences Fund
5 represented a range of about 73% to 76% of Customer Two's securities portfolio. The value of
6 the fund declined during this time period. The only other securities in Customer Two's account
7 during this time period were preferred stocks in one company.

8 22. The mutual fund investments in Customer Two's securities portfolio were not suitable
9 for her, given the lack of diversification of investments in her portfolio, the high-risk nature of
10 two of the three mutual funds, particularly the MSDW High-Yield Securities Fund, her desire to
11 preserve her investment principal, her age, her financial situation and needs, the lack of financial
12 information about her known to MERRILL, and other relevant factors.

13 Customer Three

14 23. Customer Three is a 65-year-old retired widow who lives in Goodyear, Arizona.
15 Customer Three is the mother of Customer Four. MERRILL became Customer Three's
16 stockbroker in or about October 2000. When Customer Three met with MERRILL in or about
17 October 2000, she specifically requested MERRILL explain each investment recommendation to
18 her before she gave her approval for the trade. Customer Three also informed MERRILL that
19 she was a new investor and wanted to be very conservative with her investments as she is a
20 retired widow. While MERRILL was Customer Three's stockbroker he tried to persuade
21 Customer Three to sign a discretionary agreement. Customer Three never signed a discretionary
22 agreement with MSDW and MERRILL.

23 24. From in or about November 2000 until January 2001, MERRILL made at least six
24 unauthorized trades in one or more accounts belonging to Customer Three. MERRILL made
25 many of these trades when Customer Three was out of town in November and December 2000.
26 MERRILL treated Customer Three's accounts as discretionary accounts.

1 25. Customer Three filed a complaint with MSDW against MERRILL. In July 2001,
2 Customer Three settled her claims with MSDW for a specific sum of money.

3 Customer Four

4 26. Customer Four is a 39-year-old professional woman from California who was
5 introduced to MERRILL by her mother, "Customer Three." MERRILL became Customer Four's
6 stockbroker on or about Thanksgiving Day weekend of 2000 when the two of them met.
7 Customer Four explained to MERRILL at the meeting that she was a new investor trying to learn
8 more and that she wanted to do research on trades suggested by MERRILL before authorizing
9 any transaction. Customer Four opened three accounts at MSDW. Customer Four never signed
10 a discretionary agreement with MSDW and MERRILL.

11 27. From approximately December 2000 until January 2001, MERRILL made at least
12 four unauthorized purchases in the accounts of Customer Four. At least two of these purchases
13 were transacted when Customer Four was out of the country traveling in India. MERRILL did
14 discuss two or more of these securities with Customer Four before she left on her trip to India;
15 however, MERRILL never received authorization from Customer Four to purchase these
16 securities. MERRILL treated Customer Four's accounts as discretionary accounts.

17 28. Customer Four filed a complaint with MSDW against MERRILL. In May 2001,
18 Customer Four settled her claims with MSDW for a specific sum of money.

19 Customer Five

20 29. Customer Five is an 82-year-old retired widow who lives in Sun City, Arizona.
21 MERRILL was Customer Five's stockbroker at MSDW for approximately four years. Customer
22 Five never signed a discretionary agreement with MSDW and MERRILL.

23 30. In or about September 2000, Customer Five returned home after being away on a trip
24 for about one month. After returning home, Customer Five reviewed her MSDW monthly
25 securities statement that had come in the mail while she was gone. Customer Five realized that
26 her mutual fund investment had been changed from what she believed to be a dividend growth

1 fund to what appeared to be an information fund. Customer Five did not authorize MERRILL to
2 make any trades in her account while she was away from home.

3 31. After discovering the unauthorized trades in her account, she contacted MERRILL.
4 MERRILL did not provide any explanation as to why he made the unauthorized trades in her
5 account. MERRILL did offer to reverse the trades in the dividend growth and information funds.
6 Customer Five declined to have these trades reversed because she believed she would have to
7 pay a fee. The value of the information fund declined during the time period Customer Five held
8 it in her account.

9 32. In Spring 2001, Customer Five complained to MSDW about the unauthorized trades
10 MERRILL conducted in her account. MSDW refused to remedy the situation because Customer
11 Five waited too long to complain. About two months ago, Customer Five authorized an
12 exchange of her shares in the information fund for shares in a mutual fund similar to her prior
13 investment in a dividend growth fund.

14 IV.

15 VIOLATION OF A.R.S. § 44-1991

16 (Fraud in Connection with the Sale or Purchase of Securities)

17 33. In connection with the offer to sell or buy securities, or the sale or purchase of securities,
18 within or from Arizona, MERRILL directly or indirectly: (i) made untrue statements of material fact
19 or omitted to state material facts which were necessary in order to make the statements made not
20 misleading in light of the circumstances under which they were made; or (ii) engaged in
21 transactions, practices or courses of business which operated or would operate as a fraud or deceit
22 upon customers. MERRILL'S conduct includes, but is not limited to, the following:

23 a) failing to disclose to his Customers, when communicating to them about their
24 accounts, that he had conducted unauthorized transactions in their accounts;

25 b) failing to disclose to his Customers, when communicating to them about their
26 accounts, that he had conducted unsuitable transactions in their accounts; and,

1 c) engaging in transactions, practices or courses of business which operated as a fraud
2 or deceit upon his Customers by conducting unauthorized and unsuitable transactions in their
3 accounts.

4 34. This conduct violates A.R.S. § 44-1991.

5 **V.**

6 **REVOCATION OR SUSPENSION PURSUANT TO A.R.S. § 44-1962**

7 **(Revocation or Suspension of Registration of Salesman)**

8 35. MERRILL'S conduct is grounds to revoke or suspend his registration as a securities
9 salesman with the Commission pursuant to A.R.S. § 44-1962. Specifically, MERRILL:

- 10 a) has violated the Securities Act;
- 11 b) is lacking in integrity or is not of good business reputation; and,
- 12 c) has engaged in dishonest or unethical practices in the securities industry by:
- 13 (1) executing transactions on behalf of customers without authority to do so; and,
- 14 (2) recommending, or without authorization, purchasing, selling, or exchanging
- 15 any security without reasonable grounds to believe the recommendation,
- 16 purchase, sale, or exchange is suitable for the customer considering the
- 17 customer's investment objectives, financial situation and needs, and other
- 18 relevant information that is known.

19 **VI.**

20 **REQUESTED RELIEF**

21 The Division requests that the Commission grant the following relief against MERRILL:

- 22 1. Order MERRILL to permanently cease and desist from violating the Securities Act,
- 23 pursuant to A.R.S. § 44-2032;
- 24 2. Order MERRILL to take affirmative action to correct the conditions resulting from
- 25 his acts, practices or transactions, including a requirement to make restitution pursuant to A.R.S. §
- 26 44-2032;

3. Order MERRILL to pay the state of Arizona administrative penalties of up to five thousand dollars (\$5,000) for each violation of the Securities Act, pursuant to A.R.S. § 44-2036;

4. Order the revocation or suspension of MERRILL'S registration as a securities salesman pursuant to A.R.S. § 44-1962; and

5. Order any other relief that the Commission deems appropriate.

VII.

HEARING OPPORTUNITY

MERRILL may request a hearing pursuant to A.R.S. § 44-1972 and A.A.C. R14-4-306. A request must be in writing and received by the Commission within 10 business days after service of this Notice of Opportunity for Hearing. MERRILL or his attorney must deliver or mail the request to Docket Control, Arizona Corporation Commission, 1200 W. Washington, Phoenix, Arizona 85007. A Docket Control cover sheet must accompany the request. A cover sheet form and instructions may be obtained from Docket Control by calling (602) 542-3477 or on the Commission's Internet web site at www.cc.state.az.us/utility/forms/index.htm.

If a request for a hearing is timely made, the Commission shall schedule the hearing to begin 20 to 60 days from the receipt of the request unless otherwise provided by law, stipulated by the parties, or ordered by the Commission. If a request for a hearing is not timely made the Commission may, without a hearing, enter an order against MERRILL granting the relief requested by the Division in this Notice of Opportunity for Hearing.

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Persons with a disability may request a reasonable accommodation such as a sign language interpreter, as well as request this document in an alternative format, by contacting Shelly M. Hood, Executive Assistant to the Executive Secretary, voice phone number 602/542-3931, e-mail shood@cc.state.az.us. Requests should be made as early as possible to allow time to arrange the accommodation.

Dated this _____ day of _____, 2002.

Mark Sendrow
Director of Securities